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U.S. DISTRICT COURT
DISTRICT OF DELAWARE

05- 499

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re:	Chapter 11
NORTHWESTERN CORPORATION,	Case No. 03-12872 (CGC)
Debtor.	**Hearing Date: May 17, 2004 @ 4:00 p.m.**

OBJECTION OF MAGTEN ASSET MANAGEMENT CORPORATION TO THE DEBTOR'S MOTION FOR AN ORDER PURUANT TO BANKRUPTCY RULE 9019 APPROVING MEMORANDUM OF UNDERSTANDING [DKT. NO. 1169]

Magten Asset Management Corp. (*"Magten"*), submits this objection (the *"Objection"*) to the NorthWestern Corporation's Motion for an Order (the *"Motion"*) approving the Memorandum of Understanding (the *"MOU"*) providing for settlement and dismissal of the Securities Litigation.[1] In support of its objection, Magten respectfully states as follows:

BACKGROUND

1. On September 14, 2003, the NorthWestern Corporation (the *"Debtor"*) filed with this Court a voluntary petition for relief under chapter 11 of the Bankruptcy Code. Pursuant to Sections 1107 and 1108 of the Bankruptcy Code, the Debtor is continuing to operate its businesses and manage its properties as a debtor in possession.

2. Magten holds in excess of 33% of the Series A 8.45% Quarterly Income Preferred Securities (the *"QUIPS"*) issued by Montana Capital I (the *"Trust"*). The Trust was established by The Montana Power Company, the predecessor in interest to Clark Fork and Blackfoot, LLC (*"Clark Fork"* f/k/a NorthWestern Energy, LLC). The financial obligations in connection with payment of the principal and interest on the QUIPS were subsequently assumed by the Debtor.

[1] Capitalized terms not expressly defined herein shall have the meanings ascribed to them by the Motion.

3. On March 11, 2004, the Debtor filed its Plan and Disclosure Statement with the Bankruptcy Court.

4. On March 17, 2004, Magten filed a motion for relief from the automatic stay to commence an adversary proceeding seeking to avoid the fraudulent transfer of assets from Clark Fork to the Debtor. On April 8, 2004, this Court granted Magten's motion, and on April 16, 2004, Magten filed a complaint against the Debtor in the Bankruptcy Court seeking to set aside the fraudulent transfer.

OBJECTION

A. The Motion Should be Denied Because it Seeks to Determine Issues that Should be Resolved In Connection with Confirmation of the Plan

5. By its Motion, Debtor is attempting to establish -- outside of the plan and confirmation process -- how a substantial asset of the estate is to be distributed. Through the MOU, the Debtors are seeking approval of an agreement that contemplates that creditors and equity holders with claims against the Debtor that are subordinated under section 510(b) of the Bankruptcy Code will receive distributions of estate property. If the MOU is approved, the Debtor will seek to effectuate this distribution of estate property through the Plan. In making such distributions to those creditors, to the extent any class of creditors does not accept the Plan, the Plan will violate the absolute priority rule by making distributions to junior stakeholders while paying less than 100% of the claims of more senior creditors.

6. Indeed, in explaining the standard to be applied in considering a settlement pursuant to Bankruptcy Rule 9019, the Debtor cites In re Louise's, Inc., 211 B.R. 798, 801 (D. Del. 1997), a case in which the court refused to approve a settlement and compromise because it was going to foreclose consideration of whether the Plan met the requirements for confirmation under section 1129 of the Bankruptcy Code. In In re Louise's, the court found:

> that the Settlement Agreement as a two-step or phased process would ultimately lead to a proposed plan of reorganization, the terms of which could reasonably be found to have been pre-determined by virtue of the "control" provisions of the Settlement Agreement, thereby circumventing a meaningful consideration of the requirements of Chapter 11 regarding confirmation of a reorganization plan.

Id. at 802.

7. Here too, since the Debtor is seeking to foreclose consideration of whether the distributions to subordinated creditors render the plan unconfirmable, approval of the settlement should be denied.

8. Because all of the litigation against a Debtor is stayed, and because all of the Plaintiff's claims are subordinated claims, settlements such as the one being proposed by the Debtor are very unusual. In its Motion, the Debtor fails to cite a single case that approved a settlement of a class action settlement prior to confirmation of the plan, let alone prior to approval of the disclosure statement. The only case cited by the Debtor that approved the settlement of a class action claim appears to have done so in the context of a plan. See Motion at p. 12, citing Order Confirming Third Amended Plan of Reorganization of Columbia Gas System, Inc., dated Nov 15, 1995 (Bankr. D. Del).

9. The only purpose for Debtor to pursue the settlement provided for in the MOU is to protect the Debtor's current and former officers and directors – individuals that have been accused of, among other things, material misrepresentations, breach of fiduciary duty and improperly profiting from related party transactions. The Debtor should not be using estate resources to protect individuals accused of such gross misconduct, and should not be seeking approval of such relief absent all of the safeguards attendant to the Plan confirmation process.

10. So as to ensure that the Court has a full opportunity to meaningfully consider confirmation of the Plan, to the extent the Court is inclined to grant the Motion, the order granting the relief should be conditioned upon a complete reservation of the rights of all parties in interest to object to the payment of any amounts to any creditors and to the entitlement of any creditors to receive any such payments, and to otherwise object to confirmation of the Plan on any basis.

B. The Debtor Must Clarify the Scope of the Releases Being Provided by the MOU

11. Given the breadth of the releases contained in the Plan (which will be addressed in greater detail at the Disclosure Statement hearing and the confirmation hearing) the releases contained in the MOU (the *"MOU Releases"*) raise a concern that the Debtor will assert that the MOU releases claims that are broader than provided for by the express terms of the MOU. Accordingly, to the extent the MOU is approved, it should include a provision providing that "Nothing contained herein shall release any claims of any of the holders of the QUIPS or any claims relating to or arising out of or in connection with the transfer of assets from North Western Energy, LLC (n/k/a Clark Fork and Blackfoot, LLC) to the Debtor."

WHEREFORE, Magten respectfully requests that an order be entered denying the Motion and denying approval of the MOU and granting such other relief as the Court deems just and proper.

Dated: May 5, 2004

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CERTIFICATE OF SERVICE

I, *William J. Burnett*, certify that I am not less than 18 years of age, and that on May 5, 2004, I caused service of the attached *Objection of Magten Asset Management Corporation to the Debtor's Motion for an Order Pursuant to Bankruptcy Rule 9019 Approving Memorandum of Understanding [Dkt. No. 1169]* to be made on the parties listed on the attached service list as indicated.

Under penalty of perjury, I declare that the foregoing is true and correct.

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In re:	)	
	)	Chapter 11
NORTHWESTERN CORPORATION,	)	
	)	Case No. 03-12872 (CGC)
Debtor.	)	
	)	

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Date: October 7, 2004

CASE, J.

On April 28, 2004, Debtor NorthWestern Corporation ("Debtor") filed a Motion for Order Pursuant to Bankruptcy Rule 9019 Approving Memorandum of Understanding in order to settle and dismiss all claims against it in the consolidated securities class action case *In re NorthWestern Corporation Securities Litigation,* Case No. CIV-03-4049, which included *Golman Family Trust v. NorthWestern Corp.*. Case No. CIV-03-4226, and the consolidated derivative action *In re NorthWestern Corporation Derivative Litigation,* Case No. CIV-03-4091. Referred to collectively as the "Securities Litigation," all are pending in the District Court of South Dakota.

In a nutshell, the plaintiffs in these various cases allege a variety of violations of the Securities Act of 1933 and the Securities Exchange Act of 1934 *inter alia.* Debtor, and several of its present and former officers and directors, were named as defendants. The Securities Litigation plaintiffs have filed in this case a Proof of Claim for approximately $575,000,000. The parties subsequently agreed to non-binding mediation, which resulted in the proposed settlement agreement before the Court. Under the settlement agreement, Debtor's insurers will pay from proceeds of the directors and officers policies ("D&O Policies") $37 million to the Securities Litigation plaintiffs in full settlement and compromise of the Securities Litigation and a global release of all the parties.[1] Of particular import here is the fact that no money to fund the settlement is coming from Debtor's pockets directly. The insurance proceeds being used are those proceeds from Debtor's D&O insurance policies.

There were initially two objections to the Debtor's Memorandum of Understanding –

[1]There are other entities contributing money to this settlement, but their contributions are not at issue here.

Magten Asset Management Corporation ("Magten") and Harbert Management Corporation ("Harbert"). An evidentiary hearing was held in July, 2004, after which the parties filed a series of post-trial briefs and replies/sur-replies. Harbert and Debtor have since settled, and Harbert therefore withdrew its objection. Only Magten's objection remains.

Magten holds in excess of 33% of the Series A 8.45% Quarterly Income Preferred Securities ("QUIPS") issued by Montana Capital I (the "Trust"), which was established by the Montana Power Company, predecessor in interest to Clark Fork and Blackfoot, LLC ("Clark Fork" f/k/a NorthWestern Energy, LLC). Debtor subsequently assumed the financial obligations in connection with the payment of the principal and interest on the QUIPS. Magten is pursuing a fraudulent conveyance claim against Debtor to avoid the transfer of assets from Clark Fork to Debtor.

Magten argues that the settlement agreement Debtor is proposing in effect determines outside the Plan and confirmation process how an estate asset will be distributed:

> Through the MOU, the Debtors are seeking approval of an agreement that contemplates that creditors and equity holders with claims against the Debtor that are subordinated under section 510(b) of the Bankruptcy Code will receive distributions of estate property. If the MOU is approved, the Debtor will seek to effectuate this distribution of estate property through the Plan. In making such distributions to those creditors, to the extent any class of creditors does not accept the Plan, the Plan will violate the absolute priority rule by making distributions to junior stakeholders while paying less than 100% of the claims of more senior creditors.

The critical issue raised by Magten's objection is whether the settlement payments made from the D&O policies are in fact distributions of estate property in the first instance.[2] The Court

[2]Magten further argues that the scope of the releases in the MOU should be clarified to state expressly that the claims of QUIPS holders (both as creditors and as plaintiffs in the fraudulent conveyance action) are not affected. By their terms, the MOU releases do not affect such claims and the Debtor has so confirmed on the record.

concludes they are not.

Section 541(a)(1) of the Code broadly defines property of the estate as "all legal or equitable interests of the debtor in property as of the commencement of the case." 11 U.S.C. section 541(a)(1). Generally, a debtor's liability insurance *policy* is property of the estate, *See In re Louisiana World Exposition, Inc.*, 832 F.2d 1391, 1399 (5th Cir. 1987), but whether the *proceeds* of the policy are property of the estate is in some dispute and generally hinges on the language of the policy itself and who is named as the insured. *See In re CyberMedia, Inc.*, 280 B.R. 12,16 (Bankr. D. Mass. 2002), *In re Minoco Group of Companies, Ltd.*, 799 F.2d 517, 519 (9th Cir. 1986). Where the insurance policy provides direct coverage to the debtor, the proceeds of the policy are property of the estate. *See In re Sacred Heart Hosp. of Norristown,* 182 B.R. 413, 419-20 (Bankr. E.D. Pa. 1995). Where the coverage focuses on third parties, here the directors and officers, the proceeds are not property of the estate. This Court has previously explored these distinctions in *In re Allied Digital Technologies Corp.*, 306 B.R. 505 (Bankr. D. Del. 2004).

In *Allied*, the trustee sued certain of the debtor's officers and directors. When those defendants sought to be reimbursed from the D & O policy for fees and expenses incurred in defending the case, the trustee objected, claiming that such payment would prejudice his rights as an insured under this wasting policy. The Court found that there was no meaningful direct coverage of the company but rather that the policies were in place to protect the interests of the directors and officers; therefore, the defense costs were allowed.

Here, the primary purpose of the policies is to protect the directors and officers from claims such as those asserted by the plaintiffs. However, Magten argues, without substantial

analysis, that the policies are estate property and the payment of the proceeds to plaintiffs (who are equivalent to equity holders because of the subordination provisions of Section 510(b)) would violate the absolute priority rule because the QUIPS, as creditors senior to equity, are not being paid in full.

There are three fundamental flaws with this argument. First, it ignores the difference between the policies and the proceeds of the policies. While the policies are property of the estate, the proceeds are not. Indeed, the Debtor proposes under its plan to assign its interests in the policies to a "D & O Trust" to be administered for the benefit of the beneficiaries of the policies. However, payment of the proceeds to the plaintiffs on account of claims against the directors and officers does not implicate property of the estate, as indicated above.

Second, any claims that the Debtor may have (for example, derivative claims brought on behalf of the company) are not covered by these policies because of the "insured versus insured" exception contained in them. In effect, the objection is that the proceeds under the policies should be paid to the Debtor on account of its derivative claims rather than to the plaintiffs on account of their third party claims. Although such claims may exist, they are not covered by these policies because of the exclusion noted. *See Cohen v National Union Fire Insurance of Pittsburgh, PA*, 280 B.R. 319 (Bankr. S.D.N.Y 2002). Thus, whether Debtor could or could not prevail is not relevant to this settlement because the policies at issue would not provide a source of recovery even if successfully prosecuted.

Third, any such claims of the Debtor (whether derivative or not) against the directors and officers are released under the terms of the MOU and thus the discussion above is hypothetical at best. Of course, for such a release to be valid, it must be limited in scope, reasonable and

supported by consideration. All of those conditions are met here. The scope of the releases is limited to the subject matter of the securities litigation. As consideration, the most significant element is the release of all claims of contribution and indemnification by the directors and officers against the D & O Trust to be established under the Plan. Once this settlement is funded, and other actual and estimated costs paid, approximately $13 million will remain in coverage. The elimination of potential reimbursement and contribution claims from these directors and officers is a significant benefit to the estate and the beneficiaries of the D & O trust. Finally, the Debtor itself will be released from all liability for these claims without any payment from estate funds or property.

For the foregoing reasons, Magten's objection is overruled. Based on the record at the hearing, and memoranda filed by Debtor and the Securities Plaintiffs, the Court further finds that the proposed settlement meets the requirements of approval under Rule 9019 and applicable case law. In particular, the Court finds that the resolution of this complex and expensive litigation at no direct cost to the estate is fair and reasonable, is in the best interests of the estate and its creditors, significantly enhances the Debtor's ability to emerge from these proceedings with a confirmed plan of reorganization, and is the result of arm's length negotiation.

Debtor is to submit a form of order under certification of counsel.

Charles G. Case II
United States Bankruptcy Judge

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re:	:	Chapter 11
NORTHWESTERN CORPORATION,	:	Case No. 03-12872 (CGC)
Debtor.	:	Related to Docket Nos. 1169 and 2175

ORDER APPROVING MEMORANDUM OF UNDERSTANDING

UPON the Motion For Order Pursuant to Bankruptcy Rule 9019 Approving the Memorandum of Understanding (the "Motion") filed by the above-captioned debtor (the "Debtor") and the Court having reviewed the Motion; and a hearing (the "Hearing") having been held with respect to the Motion; and the Court having heard the statements of counsel regarding the relief requested in the Motion at the Hearing; and the Court having considered the pleadings filed in connection with the Motion; and the Court having found that it has jurisdiction over this matter pursuant to 28 U.S.C. §§ 157 and 1334; and due notice of the Motion having been given under the circumstances; and it appearing that no other or further notice of the Motion is necessary or required; and the Court having determined that the relief requested in the Motion is in the best interests of the Debtor, its estate, its creditors and other parties-in-interest; and after due deliberation and sufficient cause appearing therefore, for the reasons stated in the Court's memorandum decision issued on October 7, 2004 (Dkt. No. 2175), IT IS HEREBY

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ORDERED, that the Motion[1] is **GRANTED**; and all objections to the Motion are overruled, specifically including the objection of Magten Asset Management Corporation; and it is further

ORDERED, that the Debtor is authorized to execute any documents and take any action necessary or desirable to consummate the MOU and Stipulation of Settlement; and it is further

ORDERED, that this Order shall take effect immediately upon its entry; and it is further

ORDERED, that this Court shall retain jurisdiction to hear and determine all matters arising from the implementation of this Order.

Dated: Wilmington, Delaware
October 14, 2004

THE HONORABLE CHARLES G. CASE, II
UNITED STATES BANKRUPTCY JUDGE

[1] Any capitalized term used herein but not otherwise defined shall have the meaning ascribed to such term in the Motion.